Natural Gas Market Outlook 2006-2016

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Outline

1. What should utilities do about expiring interstate pipeline contracts?
2. How much infrastructure should utilities subscribe to?
3. Should the CPUC pre-approve utility contracts with pipeline or LNG suppliers?

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What should California Utilities do About Expiring Interstate Pipeline Contracts?

- Supply diversity is important
  - Promotes gas-on-gas competition
  - Provides price stability
  - Increases infrastructure reliability
- The Rocky Mountain supply basin has a 66-year proven reserve life, the strongest production growth profile and the most attractive pricing forecast of any supply basin in the lower 48 states, including WCSB.
- California utilities have 2 Bcf/d of expiring interstate capacity, none of which is contracted from the Rocky Mountain supply area.
- Interstate capacity expansions can be accomplished economically at market tested rates and in a manner that is market responsive.

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What should California Utilities do About Expiring Interstate Pipeline Contracts? (Continued)

- Utilities must provide non-discriminatory access.
- The Commission should immediately eliminate regulatory preferences which restrict gas-on-gas competition and restrict the utilities ability to seek the most competitive supply source.
  - Order 02-06-041, requiring California utilities to acquire and preserve El Paso capacity, should be rescinded.
  - Capacity allocation proceedings on El Paso have concluded; settlement has been reached; other interstate pipelines have expanded; it is simply no longer necessary to preserve interstate capacity on El Paso and amass stranded costs which customers will have to pay.
- The order to extend these contracts to 2005 is misguided and should be rescinded.
- There is capacity available today on Kern River through capacity release and interruptible transportation programs.

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What should California Utilities do About Expiring Interstate Pipeline Contracts? (Continued)

- The designation of primary vs. secondary receipt point rights at SoCal city gates should be immediately eliminated.
  - Discriminates against new supplies and new pipelines including Rocky Mountain gas, LNG supplies and even new pipelines from the San Juan or Permian basins.
  - Restricts gas-on-gas competition and withholds lower cost gas from rate payers.
  - Disincentive to new infrastructure development, if Rocky Mountain gas is turned away from California city gates, will cause producers to seek markets to the east.
  - Physical capacity of 300 MMcf/d exists today at the Kramer Junction receipt point which is being withheld from the market because of the preferential primary/secondary receipt point distinction.

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How Much Infrastructure should Utilities Subscribe

- The lesson of the 2000-2001 energy crisis is – Don't become too dependent on the spot or secondary markets.
- Utility core requirements should be fully contracted utilizing a diverse supply portfolio including sufficient storage resources.
- Pipe is cheap – gas is expensive. Interstate transmission charges represent only 10% of the delivered cost of gas at the border. Price volatility occurs when the supply/demand balance is tight.
- Sufficient interstate pipeline infrastructure and supply diversity will produce competition among supply basins, price stability, reliability and energy security.
- Utility recontracting is an opportunity to enhance pipeline infrastructure by providing contract support for needed infrastructure investment.

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Should the CPUC Pre-Approve Utility Contracts with Pipeline or LNG Suppliers

- Utilities must have the latitude and flexibility to manage their business to meet their service obligations in a timely fashion.
- Unfortunately, we have become an industry of second guessers.
- Infrastructure investments are needed and utilities need some assurance of rate recovery to sign long-term contracts.
- Infrastructure projects by their nature require long lead times and significant capital investment. The commission must establish procedures that help expedite new infrastructure without burdening the process with exhaustive studies and analysis.
- Delays in receiving long-term contract commitments will delay needed infrastructure investments and seriously hinder California utilities efforts to diversify their gas supply portfolios.